No. 7099

IN THE

United States Circuit Court of Appeals

FOR THE

Ninth Circuit

In the Matter of Security Building & Loan Association, a Corporation,

Alleged Bankrupt,

Security Building & Loan Association, a Corporation,

Appellant,

vs.

John H. Spurlock, et al.,

Appellees.

BRIEF OF APPELLEES, Mary Rose, Ray L. Rose, Joe Ramos, Lillian M. Erwin, Luther M. Frink, E. Dale Frink, John H. Digges, Billie Lieber, Hattie M. Lieber, Hattie Schneider Lieber, Henry F. Lieber, Henry Lieber, Jr., Herman Lieber, and R. E. L. Shepherd, Receiver in Bankruptcy.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF ARIZONA

Alice M. Birdsall,
Thomas W. Nealon,
Counsel for said Appellees.

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BRIEF AND ARGUMENT OF APPELLEES, Mary Rose, Ray L. Rose, Joe Ramos, Lillian M. Erwin, Luther M. Frink, E. Dale Frink, John H. Digges, Billie Lieber, Hattie M. Lieber, Hattie Schneider Lieber, Henry F. Lieber, Henry Lieber Jr., Herman Lieber, and R. E. L. Shepherd, Receiver in Bankruptcy.

NATURE OF THE CASE

The "statement of the case" made by appellants in their brief, pages 1 to 9, with the exception of the argument and comment interjected therein, is apparently accurate and in the interest of brevity we will not repeat it here.

POINTS AND AUTHORITIES

I.

The findings of fact are sufficient to sustain the decree and no exception having been made thereto, and no assignment of error having been made that they are not sustained by the evidence, the decree should be sustained.

Sexton vs. American Trust Co., 17 A B R (NS) 36 (Iowa 8th C C A); 45 Fed. (2) 372;

Sheffield & Birmingham, C I & R Co. v. Gordon, 38 Law Ed 164; 151 U. S. 285;

Armstrong v Fernandez, 52 Law Ed 514; 208 U S 324-332.

II.

No objections or exceptions having been made to the findings of fact, nor additional findings requested, and there being no objection to the form of the judgment, the findings cannot now be attacked.

Sexton v American Trust Co. 17 A B R (NS) 36 Iowa 8th C C A); 45 Fed. (2) 372;

Sheffield & Birmingham C I & R Co. v. Gordon, 38 Law Ed 164. 151 U. S. 285;

Armstrong v Fernandez, 52 Law Ed 514; 208 U S 324-332.

III.

The findings of fact are sufficient to sustain the conclusions of law made by the court and the decree entered thereon.

IV.

No fundamental error is involved in this appeal.

V.

The appellee is not a building and loan association within the meaning of the statutes of Arizona, the common law of building and loan associations, or the exceptions in the Bankruptcy Act.

Revised Code of Arizona 1928, Sections 612 to 628 incl.

Folk, Appellant v. State Capitol Savings Assn., 214 Penn. 593.

Wilkinson v. Mutual Building & Loan Assn., 13 Fed. (2nd) 997.

Standard Savings & Loan Assn. v. Aldrich, 163 Fed 216 (6th C C A).

VI.

The appellee is not a building and loan association

in that its corporate structure does not permit the issue of a building and loan stock and does not provide for the mutuality necessary to constitute a building and loan association.

Folk, Appellant v. State Capitol Savings Assn., 214 Penn. 593.

VII.

The appellee is not a building and loan association in that it is the alter ego of the Arizona Holding Corporation, this compay owning every share of stock of the appellee and the said Arizona Holding Corporation being incompetent under the law to become a member of a building and loan association.

Phoenix Safety Investment Co. v. James, 28 Ariz., 514; 237 Pac. 958.

U. S. v. Milwaukee Refrigerator Transit Co., 142 Fed. 247.

Rice v. Sanger Bros., 27 Ariz. 15; 229 Pac. 397.

VIII.

Corporations cannot be members of a building and loan association.

Morawetz on Private Corporations, Sections 431-433.

People ex rel Peabody v. Chicago Gas & Trust Co., 130 Ill. 268.

Standard Savings & Loan Assn. v. Aldrich, 163 Fed. 216 (6th C C A).

Handlesman v. Chicago Fuel Co., 6 Fed. (2nd) 163.

Endlich, Building Associations, 2nd Ed. 323.

IX.

No presumption arises from the use of the name that the bankrupt was engaged in a building and loan association business or was in fact a building and loan association.

Rhodes v. Missouri Savings & Loan Co., 173 Ill. 621.

Meroney v. Atlanta National Building & Loan Assn., 116 N C 882.

Lilley Building & Loan Assn., 280 Fed. 143.

United States v. Freed, 179 Fed. 236.

Home Building & Savings Co., 12 B T A 289.

Acklin v. Peoples Savings Bank, 293 Fed. 393.

X.

The bankrupt is not a building and loan association or entitled to any privileges thereof, in that there has been no user of the privileges it claims.

Elgin National Watch Co. v. Loveland, 132 Fed. 41.

XI.

For sometime before the state receiver was appointed November 16, 1931, the bankrupt had abandoned all pretense of doing a building and loan business and stood revealed as a fraudulent moneyed corporation, and therefore not coming within the exception in the Bankruptcy

Act. It therefore could not claim an exemption on account of a business it had abandoned.

XII.

No corporation can claim the benefit of an exception under a statute unless it comes strictly within the exception.

United States v. Dickson, et al, 10 Law Ed. 689, 15 Peters 141.

XIII.

The appellee was organized to do something less than either a bank or a building and loan association and never did, or attempted to do, any building and loan business.

Clemons v. Liberty Savings & Real Estate Corp., 61 Fed (2d) 448 (5th C C A).

XIV.

The appellee was not a banking corporation.

Clemons v. Liberty Savings & Real Estate Corp., 61 Fed (2d) 448.

XV.

No corporation can claim to come within the exception in the Bankruptcy Act exempting it from adjudication through the doing of ultra vires acts.

Clemons v. Liberty Savings & Real Estate Corp, 61 Fed. (2d) 448 (5th C C A).

XVI.

The evidence of conduct both before and after incorporation is competent and relevant to prove fraud from the inception of the formation of the corporation.

Wood v. United States, 10 Law Ed 987, 16 Peters 342.

XVII.

The right to amend as to jurisdictional facts was duly allowed by the court upon proper showing and no error has been predicated upon the allowance thereof by the Court.

Armstrong v. Fernandez, 52 Law Ed 541, 208 U S 324-332.

ISSUES

The question raised by the Assignments of Error of appellants is the correctness of the court's decree based upon the findings of fact and conclusions of law made by the court. No error is assigned as to the sufficiency of the evidence to sustain the findings of fact. No exceptions were taken to the findings of fact and no additional findings were requested, nor were any exceptions taken to the conclusions of law, nor were any additional conclusions requested.

Insolvency was admitted by the bankrupt; also the commission of the act of bankruptcy alleged (if the bank-

rupt were not a building and loan association) and appellant's answer set up that it was a building and loan association, leaving only one issue to be tried by the court. The issues presented on this appeal are:

I.

Is the bankrupt a building and loan association within the meaning of the exception in the Bankruptcy Act exempting such an association from adjudication in bankruptcy?

II.

Were the petitions in the bankruptcy proceedings filed by the creditors sufficient to invoke the jurisdiction of the court?

STATEMENT OF FACTS

The record discloses the following facts:

In the early part of the year 1929 an application was made to the Arizona Corporation Commission to obtain a charter for the Security Building and Loan Association, one E. T. Cusick, an attorney of Tucson, Arizona, taking up the matter on behalf of the prospective organization. There are in evidence various letters and telegrams between Mr. Cusick and the Arizona Corporation Commission, and the former also testified as to his recollection of the transactions. (Transcript, pages 232-240).

The data and records produced by Cusick showed

that many months previous to the time this application was made, a corporation known as the Arizona Holding Corporation had been formed in Tucson, Arizona, and a permit to sell stock in said corporation was issued by the Arizona Corporation Commission upon condition that 80% of all moneys received from sale of the stock was to be escrowed in a bank approved by the commission (subsequently shown to be the Consolidated National Bank of Tucson), and was not to be released without the consent or order of the Arizona Corporation Commission. (Transcript, pages 241-244).

The Arizona Holding Corporation permit to sell stock was obtained from the Arizona Corporation Commission in the year 1928 upon the supposition that its purpose in selling stock was to obtain money with the expectation of organizing a building and loan association in the future. (Transcript, page 240).

On January 24, 1929, Cusick sent to the Arizona Corporation Commission certificate of the Consolidated National Bank of Tucson indicating that $53,678.61 was on deposit at that time in said bank to the credit of the Arizona Holding Corporation. (Transcript, pages 236-237). However, the records of the Consolidated National Bank of Tucson show that $14,896.67 of this amount was represented by money borrowed upon the note of certain individuals for the sum of $15,000, less interest deducted under date of January 23, 1929.

(Transcript, pages 274-275)

On March 7, 1929, there was deposited with the

State Treasurer of Arizona on behalf of Security Building and Loan Association five ten-thousand-dollar certificates of deposit of the First National Bank of Prescott, being Certificates Nos. 14, 15, 16, 17 and 18 of said bank. (Transcript, page 207).

The articles of incorporation of the Security Building and Loan Association dated March 5, 1929, and filed with the Arizona Corporation Commission March 8, 1929, recite that $45,000 of the stock of said corporation "has been subscribed to and fully paid for by the Arizona Holding Corporation." (Transcript, page 83).

A "permit" to organize as a building and loan association was issued by the Banking Department of the State of Arizona to the Security Building and Loan Association on March 12, 1929. (Transcript, page 87). The by-laws of said Security Building and Loan Association were filed with the Arizona Corporation Commission on March 8, 1929. (Transcript, page 62). These by-laws were never recorded in any county in the state. Certificate of Incorporation was issued to said Security Building and Loan Association by the Arizona Corporation Commission September 5, 1929. (Transcript, page 202).

From the minutes of said corporation it appears that an organization meeting was held March 7, 1929 at which time resignations of the five incorporators of the company, to-wit, Louis T. Beach, E. T. Cusick, W. C. Evans, J. C. Barnes and H. V. Bell, were accepted, and a resolution was passed ordering the issuance of $50,000.00 of capital stock upon payment to the corporation of the sum of $50,000. (Transcript, pages 557-562).

On March 8, 1929, Certificate No. 11 of the Security Building and Loan Association for 350 shares of its stock was issued to Arizona Holding Corporation, this certificate being under same date marked "voided", and three certificates numbered 12, 13 and 14, for 100 shares each, and one numbered 15, for 50 shares, being issued in lieu thereof, to Arizona Holding Corporation ,all under date of March 8, 1929. (Transcript, pages 480-481). No other stock was issued at that time, the only other outstanding stock as of that date consisting of the transfer from the certificates of ten shares each which had been issued to the five incorporators. (Transcript, pages 477-478).

Subsequent to this date, telegraphic communications were had between Cusick and the Arizona Corporation Commission, relative to the release of the funds of the Arizona Holding Corporation escrowed in the Consolidated National Bank, as follows:

> March 9, 1929, Cusick wired the Commission:
> "Board of Directors Arizona Holding Corporation authorize me to request immediate release of their funds in the Consolidated National Bank of this city. Wire release to bank or me immediately. Formal application follows by mail."
>
> (Transcript, page 233)

To which the Commission replied on the same date as follows:

> "Your telegram too indefinite stop Wire reason for releasing money to Arizona Holding Company stop

Do you intend to finance Security Building and Loan Association or what is the money to be used for stop Commission will not act unless fully advised."

(Transcript, page 234)

On March 11, 1929, Cusick wired the Commission as follows:

"Tucson, Ariz. 8:40 A. Mar. 11, 1929.

Arizona Holding Company has already made loans and investments subject to release of funds stop Security Building and Loan Association independent of other company has fifty thousand up with Banking Department stop Please release funds before checks are dishonored and wire release or telephone me immediately."

(Transcript, page 235)

And also sent the following telegram to the Commission the same day:

"Please immediately wire release Twenty Thousand dollars Consolidated National Bank here. This must be here before three o'clock today."

(Transcript, pages 233-234)

On March 14, 1929, Cusick wrote the Arizona Corporation Commission, the letter being headed "Re: Arizona Holding Corporation", that on the 11th he had forwarded request for release of the following funds:

Consolidated National Bank	$32,936.81
Southern Arizona Bank and Trust Company	808.59

Arizona Southwest Bank	2,888.32
	$36,633.72

stating "these sums are the amount remaining after deduction of $20,000 released by you on the 11th." Further in the letter he says: "This company (referring to Arizona Holding Corporation) is now doing business and has the opportunity to make loans and investments of advantage to it, and we respectfully urge your immediate attention to this matter."

(Transcript, pages 238-239)

March 18, 1929, the Arizona Corporation Commission wired Cusick as follows:

> "Commission authorizes release of all moneys held subject to our orders for Arizona Holding Corporation stop Have wired banks."

(Transcript, page 236)

The records of the First National Bank of Prescott and the testimony of its present cashier, P. H. Miller (Transcript, pages 204-209) disclose that on March 7, 1929, (the date of the deposit with the State Treasurer of the five certificates of deposit aggregating $50,000.00) the individual notes of Jos. E. Shreve, Glen O. Perkins and J. G. Cash, in the amount of $10,000 each, were given to that bank as part payment for the five certificates of deposit Nos. 14, 15, 16, 17 and 18, and that stock of the Security Building and Loan association was put up as collateral to the notes of Perkins and Cash. (Transcript, pages 204-206).

September 4, 1929, Certificate of Deposit No. 14 was released by the Treasurer of the State of Arizona upon the substitution by the Security Building and Loan Association of notes and mortgages in lieu thereof. October 8, 1929, the other four certificates of deposit, namely, Nos. 15, 16, 17 and 18, and the amount of $10,000.00 in mortgages and notes which had been substituted for No. 14 on September 4th were withdrawn from the State Treasurer, and a surety bond for $50,000.00 was substituted therefor. (Transcript, pages 207-209-94).

September 23, 1929, Certificate No. 14 for $10,000.00 was deposited to the account of the Security Building and Loan Association in the First National Bank of Prescott (Transcript, pages 205-207), and on October 9, 1929, Certificates Nos. 15, 16, 17 and 18, for $10,000.00 each, with accrued interest, were credited to the account of the Security Building and Loan Association in said bank, but on the same day, namely, October 9, 1929, $30,000.00 of this amount was withdrawn or withheld by the First National Bank of Prescott in payment of the three individual notes of Jos. E. Shreve, Glen O. Perkins, and J. G. Cash, each for $10,000. (Transcript, pages 205-206).

On September 21, 1929, there was assigned to Security Building and Loan Association a mortgage executed by Overland Hotel and Investment Company to William S. Millener, covering Lot 7, Block 257, Tucson, signed by Overland Hotel and Investment Company, a corporation by A. C. Shreve, Vice-President, and W. E.

Olson, Assistant Secretary, the mortgage being acknowledged September 23, 1929. The assignment of this mortgage from Millener to Security Building and Loan Association is dated September 21, 1929, and recorded October 7, 1929. (Transcript, page 211).

The property covered by this mortgage was deeded to Overland Hotel and Investment Company in 1928, subject to a mortgage of $12,000 given by Miguel Hidalgo and wife to Alianza Hispano Americana, due July 23, 1929, which mortgage was assumed by the Overland Hotel and Investment Company. (Transcript, page 664).

On October 7, 1929, the Security Building and Loan Association gave its check for $9,000 to the Arizona Holding Corporation, which check is endorsed by the latter Company to Alianza Hispano Americana Supreme Lodge. (Transcript, page 665).

The mortgage given by Hidalgo and wife to the Supreme Lodge of Alianza Hispano Americana was released on October 7, 1929.

(Transcript, page 664)

The annual report of the Overland Hotel and Investment Company dated January 26, 1929, as of the close of business April 30, 1929, shows that it was a Nevada corporation authorized to do business in Arizona, and lists as the only real estate owned by it at said time real property in Tucson, Arizona, of a value of $37,000. The report is sworn to by A. C. Shreve as Vice- President. (Transcript, pages 529-530).

The testimony of witnesses Ben Mathews and Judge E. R. Chambers of Tucson, at the trial of the case, identified the property covered by this mortgage as being property in the business district of Tucson adjoining the Santa Rita Hotel on which was located a garage, and the former placed its value in September, 1929, as from $30,000 to $32,000. (Transcript, page 277), and the latter placed its value at the same time as from $20,000 to $22,000.

(Transcript, page 285)

On or about October 22, 1929, a corporation known as the Century Investment Trust was organized, the incorporators being Glen O. Perkins, A. C. Shreve and V. Munter. The officers of said Century Investment Trust as shown by the report filed with the Arizona Corporation Commission June 30, 1930, are the following: President, J. H. Shreve, San Diego, California; Vice-President, D. H. Shreve, Phoenix, Arizona; Secretary, J. R. DeLatour, San Diego, California; Assistant Secretary, Glen O. Perkins, Phoenix,. Arizona.

(Transcript, pages 525-527)

November 15, 1929, Certificate No. 12 for 100 shares of Security Building and Loan Association stock issued to Arizona Holding Corporation on March 8, 1929, was endorsed to Century Investment Trust (Transcript, page 481), and the same condition exists with respect to Certificate No. 13 (Transcript, page 481). These 200 shares are transferred on the stock book and represented by Certificate No. 18, for 200 shares issued November 15,

1929, to Century Investment Trust (Transcript, page 483). Certificate No. 15 for 50 shares issued to Arizona Holding Corporation March 8, 1929, was endorsed to Century Investment Trust April 5, 1930, (Transcript, pages 482-483), and is presumably represented by Certificate No. 23 for 50 shares issued to Century Investment Trust December 16, 1930. (Transcript, page 485). Certificate No. 14 for 100 shares issued to Arizona Holding Corporation March 8, 1929, was endorsed to Century Investment Trust April 5, 1930, (Transcript, page 482), and is represented by Certificate No. 24 issued to Century Investment Trust September 4, 1931. (Transcript, page 485).

The stock sale report of the Century Investment Trust made to the Arizona Corporation Commission for the period from October 29, 1929, to December 31, 1929, inclusive, (Transcript, page 532) shows A. C. Shreve as having bought 250 shares of stock, paying to himself a commission of $50.00 thereon, and Glen O. Perkins as having bought 250 shares of stock, also paying to A. C. Shreve a commission of $50.00. Certificate No. 4 shows stock sale to Century Corporation of 530 "B" Street, San Diego, reported as cash received $42,000.00. Certificate No. 5, for 35,000 shares of common stock, together with Certificate No. 1 for 50,000 Series "A" stock, is listed as sold to Century Corporation of San Diego under title "Exchange of Stock". Certificate No. 37 for 1368 shares preferred stock, with Certificate No. 40 for 1368 shares of common stock, likewise goes to Century Corporation of San Diego assertedly for $34,200.00 cash. Certificate No.

98 for 1416 shares preferred, with Certificate No. 113 for 1416 shares common stock is listed to the same company at an alleged cash receipt of $35,400.00. Certificate No. 99 for 4,000 shares preferred, with Certificate No. 114 for 4,000 shares common, and Certificate No. 118 for 400 shares Series A is listed as sold to Arizona Holding Corporation for cash receipt of $100,000.00.

(Transcript, page 533)

From the date of its organization the capital stock of the Security Building and Loan Association, outside of the few shares issued for qualification for voting purposes of directors, and for which no consideration was paid, was held by the Arizona Holding Corporation until about the 15th day of November, 1929, and from that time on was held by the Century Investment Trust.

(Transcript, pages 477-486)

In November, 1931, there were issued and outstanding of the capital stock of the Security Building and Loan Association 450 shares, of which 420 shares were held by the Century Investment Trust and John C. Hobb Glen O. Perkins and D. H. Shreve, each held ten shares. (Transcript, pages 477-486).

Paragraph VI of the Articles of Incorporation of the Security Building and Loan Association reads as follows:

> "That the amount of capital stock of this corporation is Five Million ($5,000,000.00) Dollars, and the number of shares into which it is divided is Fifty Thousand (50,000) of the par value of One Hundred

($100) Dollars each, all of which, when issued, shall be set apart as a fixed and permanent guaranteed capital. Additional working capital may be accumulted by the issuance of membership shares, units and certificates, both installment and fully paid as provided for in Chapter 76, 1925 Arizona Session Laws, and the By-Laws of this Corporation."

(Transcript, page 83)

This paragraph is followed by a paragraph in which it is stated that the amount of said capital stock which has been actually subscribed is $45,000.00, and the whole thereof has been subscribed to and fully paid for by the Arizona Holding Corporation, a corporation organized and existing under and by virtue of the laws of the State of Arizona.

(Transcript, page 83)

Article II of the By-Laws of said corporation relating to capital stock reads as follows:

"Capital Stock

Section 1. The capital stock of this corporation shall be Five Million ($5,000,000.00) Dollars divided into Fifty Thousand (50,000) shares of a par value of One Hundred ($100) Dollars each, all of which shall be a capital, and shall be issued at such times and in such amount as the Board of Directors may determine. It shall be sold upon subscription, at not less than par, payable not less than 50% at the time of subscription, and the balance as may be ordered by the Board of Directors. This stock is not withdrawable until final liquidation, and no loans shall

ever be made upon the pledge of any of its shares, as security, to the corporation.

Section 2. The majority of the Board of Directors shall always be selected from those holding ten or more shares of capital stock, and the minority may be selected from holders of membership shares.

Section 3. The capital stock shall participate in the net earnings of the association to the full extent permitted, or which may be permitted, under the provisions of the laws of the State of Arizona, and as interpreted by the Arizona Corporation Commission and/or the State Superintendent of Banks."

(Transcript, pages 63-64)

The "membership shares" of the Association are covered in Article VIII as follows:

"Membership Shares

Section 1. Membership shares having an ultimate matured or par value of One Hundred ($100) Dollars each *may* be issued *at such time and in such manner as the Board of Directors may prescribe,* or in accordance with the terms and provisions of the charter of this corporation.

Section 2. Membership shares may be classified as installment or full pay. Each subscriber to the installment shares shall become entitled to said shares when the payments made thereon, together with the profits apportioned thereto, shall amount to the sum of One Hundred ($100) Dollars for each of such shares, at which time the shares shall mature and

payments thereon shall cease. Full paid membership shares may also be issued at such times as the Board of Directors may determine to subscribers paying in the full face value of One Hundred ($100) Dollars per share. Dividends at such rate per annum as may be fixed by the Board of Directors, not exceeding a full participation in the net profits, shall be paid on these shares.

Section 3. Holders of either form of membership shares are members of the corporation, with all the rights, powers and privileges incident thereto, including the right to vote at all meetings of the shareholders and members—one vote for each share—and are subject to the same restrictions and liabilities.
Section 4. An entrance fee of not exceeding Two Dollars ($2) per share may be charged and collected upon all installment membership shares." (Italics Ours).

(Transcript, pages 71-72)

No action was ever taken by the Board of Directors authorizing issuance of any membership shares under the provisions of Article VIII of the By-Laws as appears from the minutes of said corporation (Transcript, pages 554-631), and no stock book or other record shows issuance of any such shares (Transcript, page 486).

Article IX of the By-Laws entitled "Investment Certificates" provides for the issuance of pass book as well as additional forms of investment certificates. (Transcript, pages 72-74). These various forms of investment certificates appear in the record.

(Transcript, pages 212-221)

Section 3 of Article IX of the By-Laws provides as follows:

> "Section 3. Holders of any of the forms of Investment certificates above designated are not members of the corporation, and have none of the rights, powers and liabilities incident thereto."

(Transcript, page 74)

In Section 1, subdivision 5, Article IV of the By-Laws entitled "Power and Duties of Directors" appears the following provision:

> "To borrow money for the purpose of making loans or with which to pay withdrawals or maturities".

(Transcript, page 66)

At a special meeting of the Board of Directors of the Security Building and Loan Association held on September 30, 1931, action was taken by said corporation whereby all real estate mortgages and contracts owned by the Security Building and Loan Association were transferrel to Century Investment Trust, a corporation, in consideration of a note to be given by said Century Investment Trust, a corporation, to said Security Building and Loan Association, payable in monthly installments of $2,500.

(Transcript, pages 626-627)

Said deal was consummated as of date October 1, 1931, the note received by said Security Building and

Loan Association being in evidence (Transcript, pages 265-266) and reading as follows:

> "$250,427.45 Phoenix, Arizona, Oct. 1, 1931. In monthly installments after date, for value received, we promise to pay to Security Building and Loan Association, or order, at Phoenix, Arizona, the sum of Two Hundred Fifty Thousand Four Hundred Twenty-seven and 45/100 Dollars, in monthly installments of Twenty-five Hundred Dollars and no/100th each, on or before the last day of each and every month following the date hereof until the entire sum shall have been paid with interest hereon from date at the rate of seven per cent (7%) per annum, payable monthly; said interest to be deducted from the monthly payment; principal and interest payable in lawful money of the United States. We hereby deposit with said Security Building and Loan Association as collateral, security for the payment of this note, mortgages and contracts on real estate as per list hereto attached.
>
> (Signed) Century Investment Trust,
>
> By D. H. Shreve, President,
>
> By Glen O. Perkins, Secretary."

On November 14, 1931, the Superintendent of Banks cancelled the permit of the Security Building and Loan Association to do business in Arizona. (Transcript, page 90).

On November 16, 1931, a Receiver was appointed for said Security Building and Loan Association by the Superior Court of Maricopa County, Arizona, in a suit

filed on the same day, this being the admitted Act of Bankruptcy on which the adjudication in Bankruptcy is predicated.

Some of the outstanding facts developed may be summarized as follows:

1. No stock of the Security Building and Loan Association was ever issued except capital stock to the amount of 450 shares, and this capital stock was never paid for.

2. There were no members of the Security Building and Loan Association, and no membership shares were ever issued.

3. No loans were ever made to members, in accordance with the provisions of the statute requiring every borrower to subscribe for shares of the company in an amount equal to the loan.

4. Withdrawals of funds deposited were allowed without notice and contrary to the provisions of the statute. In fact, money was borrowed from the banks by order of the Board of Directors to pay withdrawals.

5. All of the stock of the company, with the exception of thirty shares, was held by interlocking companies.

6. All of the assets of the company were transferred to the Century Investment Trust on October 1, 1931, in exchange for the note of that company, so that on November 14, 1931, the date of the commission of the al-

leged act of bankruptcy, the only asset of the Security Building and Loan Association was a promissory note of the Century Investment Trust.

BRIEF OF ARGUMENT

ISSUE NO. I., covering appellant's specifications of Error Nos. I and III (Assignments of Error Nos. I, II and III).

The court's finding of fact is sufficient to support the decree (T R 183-190), and no additional finding was requested. The pleadings being sufficient on their face to give the trial court jurisdiction, we do not think it is incumbent on this Court, in the absence of an Assignment of Error, to examine the evidence to see if the finding is supported by the evidence. We submit that the evidence does support the finding.

The evidence shows that the corporation was fraudulent in its inception; that the corporation was never formed with the intention of doing a building and loan business, but was a mere mask to defraud the public and particularly the people of Tucson and Phoenix, Arizona, through a fraudulent use of the mails for the aggrandizement of those who formulated the fraudulent scheme. Its Articles of Incorporation and corporate structure preclude the idea of its being a building and loan association or doing a building and loan business.

It was the alter ego of another corporation (The Arizona Holding Corporation) which owned all its capital

stock and which was not exempt from adjudication in bankruptcy, all of which is shown by the following evidence:

1. The individuals who devised the fraudulent scheme and consummated the fraud to the extent of defrauding the public to approximately $190,000.00, are:

Jesse H. Shreve,
A. C. Shreve,
Joseph E. Shreve,
Dan H. Shreve,
Glen O. Perkins,
J. G. Cash,
F. D. Arrington,
W. C. Evans,
W. E. Oleson,
W. S. Millener,
E. R. Kelly,
Valeria Munter,
J. R. DeLatour.

These, together with certain of their associates and employees carried out the fraudulent schemes.

2. The corporations involved having identity of ownership, or almost identical ownership, were:

Arizona Holding Corporation, owner of all of the stock of the bankrupt corporation;

Security Building and Loan Association, Bankrupt;

Century Investment Trust, organized by the same

group for the purpose of consummating the fraud;

Sunset Building and Loan Association of San Diego, California, one of the principle beneficiaries of the fraud;

Overland Hotel & Investment Company, whose officers manipulated the $30,000.00 fraudulent mortgage transaction;

Century Corporation, utilized in the exchanging of stock and padding of assets;

Southwest Securities Company, Shreve controlled;

3. The relationship of the parties to the various corporations was as follows:

J. H. Shreve, 546 B Street, San Diego, California:

Principal promotor of the Arizona Holding Corporation (T R 239-240);

Stockholder and owner of Certificate No. 1 for $10,000.00 (Pet. Ex. 51, photostatic insert between T. R. 530-531).

(Commission paid Glen O. Perkins on this transaction $2,000.00).

President and Director of Security Building & Loan Association (T R 462, 519, 559, 563, 564, 580, 583, 584, 588, 591, 599, 600, 604).

Chairman of Security Committee of Bankrupt (T R 586).

Chairman of Finance Committee (T R 586).

Appraiser for bankrupt (T R 587).

Promoter and endorser of note to procure original deposit, being one of the early frauds in the scheme (T R 206).

Endorser on Glen O. Perkins note, a part of same fraudulent transaction (T R 206).

Endorser on note of J. G. Cash (T R 206), part of same fraudulent transaction;

Pledger of 200 shares of Sunset Building and Loan stock, part of same transaction (T R 206).

President of Century Investment Trust (T R 527).

A. C. Shreve:

Vice-president and Director of Security Building & Loan Association (T R 221, 462).

Holder of $10,000.00 of stock of Arizona Holding Corporation (T R 531).

Vice-president of Arizona Holding Corporation, and the person who verified the report, Petitioner's Exhibit 49 (insert p. 531).

Incorporator of Century Investment Trust (T R 527).

Vice-president Overland Hotel & Investment Co. (T R 530, 566).

Assignee Yuma County fraudulent mortgage (T. R. 671).

Mortgagee in fraudulent Yuma County mortgage (T R 673).

Releasor fraudulent Yuma County mortgage (T R 673).

Joseph E. Shreve, Southwest Securities Company, San Diego, Calif.

One of those who borrowed money from First National Bank at Prescott for original deposit and deposited 100 shares of Sunset Building and Loan stock as collateral thereto, thus aiding the institution of the fraudulent corporation; (T R 205).

(The above note is endorsed by Jesse H. Shreve.)

Dan H. Shreve,

President, Director and active manager of bankrupt corporation during the latter days of its activity and participant in numerous fraudulent transactions hereafter enumerated (TR 103).

The individual who swears to bankrupt's answer as president of the corporation (T R 103).

Signer of fraudulent note of $250,429.45 together with Glen O. Perkins, to Century Investment Trust (T R 266).

Signer of many fraudulent appraisals, including one on 240 acres of desert land in Yuma County at $650 per acre, the actual value of the land being $10.00 per acre. This appraisal recites two buildings upon premises, with insurance of $9,-500.00 whereas there are actually no buildings on the premises (T R 333 to 361, inc.)

Fraudulent participant in Dreyfus, Arrington and Shumway loans (T. R. 350, 351).

Signer of J. M. Shumway check for $7,000.00, thereby fraudulently extracting $7,000.00 from the

assets of the bankrupt corporation (T R 497).

One of the individuals who induced J. M. Shumway, an employee, to sign blank notes and mortgages and thereafter set up a fraudulent loan thereon by means of which the bankrupt corporation was defrauded of $2,715.00, in addition to the above amount; (Insert opposite T R 497).

Vice-president of Century Investment Trust (T R 527).

President of Arizona Holding Corporation (T R 524).

Glen O Perkins:

Secretary and director of bankrupt corporation (T R 394, 563).

Assistant secretary Century Investment Trust (insert p. 533).

Incorporator of Century Investment Trust (T R 525).

Assistant secretary of Arizona Holding Corporation (T R 524).

An active participant in practically every fraudulent transaction.

E. R. Kelly:

A Director of bankrupt corporation; (T R 559).

Secretary and treasurer of Overland Hotel & Investment Co. (T R 530).

Participant in $30,000.00 fraudulent mortgage trans-

action (T R 530).

J. R. DeLatour:

Director of bankrupt corporation (T R 563, 631) Secretary Century Investment Trust (T R 527).

J. G. Cash:

Secretary and director of bankrupt corporation (T R 631).

Secretary of Arizona Holding Corporation (T R 524).

Valeria Munter:

Secretary of Overland Hotel & Investment Co. (T R 531).

Incorporator Century Investment Trust (T R 525).

F. D. Arrington:

Vice-president Overland Hotel & Investment Co. (T R 530).

Mortgagor who executed fraudulent mortgage of $34,000.00 on 120 acres of Yuma County desert land, not worth to exceed $10.00 per acre. (T R 674).

W. C. Evans:

Director of bankrupt corporation. (T R 83).

Participant in original fraudulent transaction in regard to procuring instruments for deposit with State Treasurer to secure license for bankrupt

corporation (T R 207 insert).

Incorporator of bankrupt; (T R 80).

W. E. Olson:

Assistant Secretary of Overland Hotel & Investment Company; (T R 211).

Signer of $30,000 mortgage (T R 211).

W. S. Millener:

Payee in $30,000.00 Overland Hotel & Investment Co. mortgage and assignor thereof (T R 211).

4. The methods by which the creditors of the bankrupt corporation were defrauded were as follows:

a) By obtaining control of the Arizona Holding Company when the promotors thereof were unable to raise the necessary capital and had only raised $36,000.00 out of the necessary $50,000.00.

b) By using a phony check of the Arizona Holding Corporation through the First National Bank of Prescott, Arizona, for $20,000.00, thus deceiving the attorney in charge of procuring the Articles of Incorporation for the bankrupt, and thereby causing him unintentionally to deceive the Arizona Corporation Commission as to the capital being paid in;

c) By putting up notes secured by stock not yet issued as collateral for $30,000.00 as a step in

the organization of the bankrupt without paying in any money on their capital stock;

d) By subsequently giving the bankrupt corporation's check for $30,000.00 on the First National Bank of Prescott to pay the individual notes of Joseph E. Shreve, Glen O. Perkins and J. G. Cash from the funds of the corporation;

e) By transferring from the funds of the bankrupt the sum of $9,000.00 to the Arizona Holding Corporation;

f) By transferring a $30,000.00 mortgage of the Overland Hotel & Investment Company to the bankrupt corporation upon a false appraisal of the property.

g) By the execution of fraudulent and dummy loans, extracting a further sum of many thousand dollars from the funds of the bankrupt corporation;

h) By assigning the above mentioned $30,000.00 mortgage to the Sunset Building and Loan, making a mere charge thereof on open account for same;

i) By false appraisals of property for the purpose of dummy loans;

j) By transferring much of the funds of the corporation to the Century Investment Trust;

k) By transferring much of the funds of the corporation to the Arizona Holding Corporation;

l) By deceiving the Banking Department of the State of Arizona and the State Treasurer of Arizona by false appraisals and false financial reports, thereby procuring license to operate as a building and loan association, including in said reports the issuance of fire insurance on non-existing buildings;

m) By transferring notes and mortgages of the face value of $250,427.45 to the Century Investment Trust in a fraudulent transaction;

n) By transferring mortgages, notes, etc., to the Sunset Building and Loan Association without consideration;

o) By inducing employees to sign notes and mortgages in blank, filling them in for fictitious values and extracting the money represented thereby from the assets of the corporation and reporting these as actual loans to the Banking Department of the State of Arizona;

p) By false transfers and exchanges of stock to bolster up the assets of the allied corporations;

q) By fictitious entries of payments of commissions on sales of stock in allied corporations;

r) By obtaining property of individuals through the issuance of fraudulent stock and manipulating same, placing dummy mortgages thereon, to withdraw funds from the assets of the bankrupt corporation; the assets going to the fraudulent promoters of this scheme;

s) By making excessive loans on churches and night clubs as a bait to the public, all in violation of the building and loan statutes;

t) By sending false and misleading circulars through the mail in aid of its fraudulent schemes and using the names of Chief Justice Hughes, ex-President Coolidge, and President Hoover, in a connection indicating that they endorsed the fraudulent schemes that were being perpetrated upon the public;

u) By releasing mortgages and having deeds made to the Arizona Holding Corporation to the extent of the face value of $110,000.00, on the eve of collusive receivership proceedings, thereby depriving the bankrupt corporation of valuable assets.

BANKRUPT NOT A BUILDING AND LOAN ASSOCIATION UNDER ITS ARTICLES OF INCORPORATION.

(a) The purposes set forth in the Articles of Incorporation are contrary to the Building and Loan Act. It was simply an ordinary corporation formed for the purpose of fraud and misleading the public into thinking that it was a building and loan association.

(b) Its by-laws did not comply with the building and loan statute and were never recorded as required by the Act.

(c) Its by-laws do not even attempt to comply with the Building and Loan Act.

(d) Article II of its Articles of Incorporation provide that the capital stock should be $5,000,000, divided into 50,000 shares of the par value of $100.00 each. The stock so provided for consists of ordinary corporate stock and that being the full extent of its authorized capital it could not without amendment of its Articles issue building and loan stock (T R 83).

(e) Article VII of its Articles of Incorporation provides as follows:

> "That the amount of said capital stock which has been actually subscribed is $45,000.00 and the whole thereof has been subscribed and fully paid for by the Arizona Holding Corporation, a corporation organized and existing under and by virtue of the laws of the State of Arizona." (T R 83).

(f) Article II of its By-laws provides that the stock provided for in Article VI of the Articles of Incorporation shall be sold upon subscription at not less than par, payable not less than 50 percent at the time of subscription and the balance as may be ordered by the Board of Directors.

> "This stock is not withdrawable until final liquidation and no loan shall ever be made upon the pledge of any of its shares as security to the corporation." (T R 63).

(g) Article IX of the By-laws provides for the issuance of investment certificates, something that is not authorized, nor contemplated in the Building and Loan Act of Arizona. (T R 72, 73, 74).

(h) Article XIV of the By-laws recites that the Arizona Holding Corporation is the owner of all of the subscribed shares of stock in the Security Building & Loan Association at Tucson, Arizona, except such as are subscribed and paid for by the incorporators. (T R 79). The record shows that no shares were paid for by the incorporators and that those that were issued to them were immediately transferred in blank and delivered back to the corporation.

(i) Article II of the Articles of Incorporation show a plan of accumulating funds contrary to the letter and spirit of the Building and Loan Statutes of Arizona (T R 81).

(j) The Articles fail to provide for any form of stock required by Section 612, Revised Code of Arizona, 1928.

NO USER OF ANY BUILDING AND LOAN PRIVILEGE

The corporation did not make any user of any building and loan feature of its Articles of Incorporation:

It accumulated no funds from members as provided for in Section 612 of the Code;

It invested no fund in loans to its members upon real estate for home purposes as provided in said Section;

It did not permit its members to elect directors as provided in Section 615;

It did not confine its loans to notes secured by first mortgage on improved real property or real property to be improved under contract with the Association as provided by Section 618;

It paid no attention to the restriction in said Section that its loan should not exceed sixty per cent of the conservative market value of the improved real property;

It made no loans in accordance with the requirements of said Section 618 that "no loan shall be made except upon the report in writing of three appraisers who shall be members of such Association and who shall report the conservative value of the property to be mortgaged."

It did not require its borrowers at the time of procuring a loan, or at any other time, to subscribe for an amount of stock in the Association equal to its loan, or provide that any such stock should be held as further security for said loan as provided for in said Section 618;

It had no members.

In general it did not attempt in any manner to comply with the provisions of Article IV of the Arizona Code of 1928, or of the Session Laws of 1925 under which it purported to be organized.

ARGUMENT

ISSUE NO. 1.—Specifications of Error Nos. I and III, (Assignments of Error Nos. I, II and III):

The bankrupt corporation does not come within any of the accepted definitions of a building and loan association, either in its corporate structure or its method of doing business, even if we should consider it separate and apart from its alter ego, the Arizona Holding Corporation, and even if we should eliminate the fact that it is a corporation fraudulent in its inception, designed and incorporated for the purpose of carrying out a mail fraud scheme; that all its operations from its first application for a certificate of incorporation to its last corporate act were fraudulent.

The facts in evidence as stated in the Transcript of Record and pointed out in this brief, show clearly that there was fraud from the inception of the corporation. This is proved by its conduct prior to the time of the granting of any right as a corporation by the State and by all of its subsequent acts, and under the rule laid down by Judge Story in Wood v United States, 10 Law Ed, 987, 16 Peters 342, fraud in the inception may be proven by the conduct subsequent, as well as by the prior conduct of the parties.

> "The other objection has as little foundation, for fraud in the first importation may be as fairly deducible from other subsequent fraudulent importations by the same party as fraud would be in the last importation from prior fraudulent importations. In each case the *quo animo* is in question, and the presumption of fraudulent intention may equally arise and equally prevail."
>
> *Wood vs. United States,* supra.

The outstanding characteristic of a building and loan association is mutuality. Without this quality there can be no such thing as a building and loan association whatever name it may travel under. The name itself does not give it this character.

> "It is merely a money lending dividend paying corporation, to which for some purpose, features of a building and loan association have been attached. The purposes and powers put it outside of the pale of the beneficent statute which was intended to encourage co-operation among the saving poor and not to aid the rich in finding good investments for their capital."
>
> *Rhodes v. Missouri Savings & Loan Co.* 173 Ill. 621.

The above quotation is taken from the case of Meroney vs. Atlanta Building & Loan Assn., 116 N. C. 882, 47 A. S. R. 841, quoted with approval in the Illinois case. The Illinois court continues:

> "A true building and loan association such as our statute provides for has no authority to declare or pay dividends on its stock. Instead of its funds being derived from small payments made monthly by its subscribers it may instead derive its entire fund by large subscriptions of thousands of dollars made by money lenders and capitalists, who thus in the guise of subscribers to stock in a so-called 'building association' are enabled to realize thirteen or fourteen percent interest on money invested. * * * Neither directly nor by implication is the issue of paid-up stock recognized by our statute."

and the Illinois court continuing thus distinguishes between such a corporation and a building and loan association:—

> "From this reasoning it may be concluded that an association which under the *GUISE OF A BUILDING AND LOAN ASSOCIATION* (ITALICS ours) derives its funds for loaning from the issue of what is known as 'paid-up stock' in the sum of $1,000.00 or from any other form of paid-up stock not authorized by the statute of this state to be issued by such an association and whose business is of such character as *MAKE IT IN FACT A LOAN COMPANY* (ITALICS ours), will be treated as such a company and will not, in the absence of other additional legislation, receive the benefits of the liberal statutes and decisions in this state which have attempted to foster these purely co-operative associations for building and saving purposes."

The Illinois Court quotes with approval from the case of Andrews v Poe, 30 Maryland, 485 (a case where the aim and purpose of the association did not bring it within the statute as a building association):

> "Every device and shift which the wit of man could suggest have been invoked to exempt contracts for illegal interest from the operation of the law, but courts should look under the mask to discover the true nature of the transaction."

A building and loan corporation is defined by Section 612 of the Civil Code of Arizona, 1928, as:

> "Organizations having for their object accumulations

by its *members* of their money by periodical payments into the treasury thereof to be invested from time to time in loans to the *members* upon real estate for home purposes." (Italics ours).

This is the accepted definition of a building and loan association. So a corporation formed for the purpose of accumulating its funds by payments from those other than its members or those who could not under the law become its members, and for the lending of money to persons who are not members or who could not become members, and loans not made for home purposes, cannot come within the definition prescribed by the statute.

The Section above referred to is the same as Section 1, Chapter 76, Session Laws of 1925.

Judge Endlich, the author of the accepted standard work on building and loan associations, in his opinion in the case of FOLK, APPELLANT vs. STATE CAPITAL SAVINGS ASSOCIATION, 214 Penn. 593, states the essential qualities in very clear language:

"It is, indeed, to be noted that the legislature has attempted no definition of what constitutes a building association. It has assumed that certain features and methods are essential to it, and there is no room for doubt that without them no corporation, whatever its label, can claim to be a building association. But it has not excluded the possibility that consistently with these essential features the legitimate development of the business of these associations may add others which at the date of the enactment were not foreseen and against which there-

> fore is not to be taken as implying any prohibition. Thus it is well understood to be one of the differentiating characteristics of the building association scheme that it affords an opportunity to shareholders to subscribe for stock payable in small periodical installments. A society discarding this feature could hardly be looked upon as within any definition of building association."

The feature which Judge Endlich was pointing out that might be added in addition to the stock payable on these installments was that the corporation could in a proper case allow to paid-up shareholders a periodical dividend, reasonably within the margin of profit shown by experience to be likely to accrue to the society on the sum thus paid, which dividend is understood to be payable only out of the profits earned and in lieu of any share therein upon winding up.

In this corporation every share of stock was owned by the Arizona Holding Corporation, an entity that was incapable of becoming a member of a building and loan association.

The rule is laid down in Endlich, Building Associations, (2nd Ed) p. 323, and is cited with approval in Handelsman v. Chicago Fuel Company, 6 Fed (2) 163, Judge Endlich's language being as follows:

> "It certainly does not appear to be consistent with the purpose of a building association's being, nor in any wise related to the policy which justifies the creation of these institutions, with the extraordinary powers they possess, *TO HAVE ITS MEMBER-*

SHIP IN PART COMPOSED OF CORPORATIONS, and there can be little doubt that the statutes never contemplated such a departure. (ITALCS ours).

We quote also from the decision by Judge Lurton in the case of Standard Savings & Loan Association vs. Aldrich, 89 C C A 646, 163 Fed. 216, wherein he says:

> "The investment of funds in the shares of a company organized for a like purpose is beyond the scope of the most liberal view of the incidental or implied power of such companies. The objects of such associations being only to lend the funds contributed by members for the purpose of building and improving homesteads, one such association could not become a member of another, nor could it lend its own funds except to its own members for the purpose indicated. The contention, therefore, that the Michigan Association could not legally become a member of the Standard Association, and that the latter could not legally lend its money to an association which was not and could not lawfully become a member, has not been inadvertently made. Thomps. Bldg. & L. Assn. 2d ed. p. 215 Sec. 114; 4 Am & Eng Enc Law, 2d ed. p. 1028; Kadish v Garden City Equitable Loan & Bldg. Assn. 151 Ill. 531, 42 Am. St. Rep. 256, 38 N. E. 236; North American Bldg. Assn. v. Sutton 35 Pa 463, 78 Am. Dec. 349; Mechanics & W. Mut. Sav. Bank & Bldg. Assn. v. Meridan Agency Co. 24 Conn. 159".

See also the following authorities:

Morawetz on Private Corporations, Sections 431-432.

People ex rel Peabody v. Chicago Gas & Trust Co., 130 Ill. 268.

The Articles of Incorporation of this association provide for a capital stock of $5,000,000.00, all of one class, and that class the kind issued by any corporation incorporated under the general law; therefore, within its authorized capital it would have no authority whatsoever to issue membership shares. This could not be done unless it amended its Articles of Incorporation. For this reason it necessarily follows that it could have no members, could make no loans to members, and could not organize as a building and loan corporation as it purports to be from its name. That the name does not add anything to its character as a building and loan association, unless it has the essential qualities heretofore mentioned, is held in the following cases:

Rhodes v. Missouri Savings & Loan Co. 173 Ill. 621.

Meroney v. Atlanta National Bldg. & Loan Assn., 116 N. C. 882, 47 A. S. R. 841.

Lilley Building & Loan Assn., 280 Fed. 143.

United States v Freed, 179 Fed. 236.

Home Building & Savings Co., 12 B T A 289.

Acklin v. Peoples Savings Bank, 293 Fed. 393.

Every share of stock of the bankrupt being owned by the Arizona Holding Corporation, the bankrupt is merely the alter ego of the Arizona Holding Corporation, and for this reason cannot claim any privilege or exemption to which the Arizona Holding Corporation could not assert

a claim. Therefore, it being the alter ego of the Arizona Holding Corporation, as the facts and evidence clearly show, it could not claim to come within the exception in the Bankruptcy Act exempting building and loan associations from adjudication in bankruptcy.

The court having made its findings of fact, no exceptions being taken thereto, and no additional findings of fact being requested, we do not know how far the court may desire to go into the evidence. It is true that one of the facts to be found by the court was the jurisdictional fact that this corporation was not a building and loan association within the meaning of the Bankruptcy Act. However, this is a question of fact which the court had the jurisdiction to determine. It is not our conception of the law that it is the duty of the Appellate Court to wade through all of the testimony to ascertain whether the trial court made its finding of fact thereon upon sufficient testimony when there is no assignment of error that there is no evidence to support the finding of fact.

Armstrong vs. Fernandez, 52 Law Ed 514; 208 U S 324-332.

The bankrupt having been organized for a fraudulent purpose as the facts and evidence show, then the Court will disregard the corporate form in the interest of justice. This is as applicable to a situation where one corporation is the alter ego of another as it is in the case of individuals.

"Aside from the question as to whether or not The

French Shop Inc., was a corporation *de facto,* in this case it appears to us that we should apply a rule which has received the recognition of text-writers and courts, generally, viz., that a corporation may not be formed for the purpose of perpetrating a fraud or other illegal act, under the guise of the fiction that a corporation is a legal entity, separate and distinct from its members. *WHEN THIS IS ATTEMPTED, THE FICTION WILL BE DISREGARDED BY THE COURTS, AND THE ACTS OF THE REAL PARTIES DEALT WITH AS THOUGH NO CORPORATION HAD BEEN FORMED.* Cook on Corporations, vol. 3, 7th ed., Sec. 663; Donovan v. Purtell, 216 Ill. 629, 1 L. R. A. (N.S.) 176, 75 N. E. 334; 14 C. J. 61, Sec. 22, and cases cited.

"The more is the reason for this rule where the *INCORPORATORS* are themselves the *ALTER EGO* of the corporation, and the persons sought to be held as partners are the sole owners of the capital stock, and the sole managers and directors of the company. In this case the Rices were themselves the corporation. While the evidence of fraud as to the original purpose of the organization of the corporation is not so direct and plain as to be conclusive, yet the facts and circumstances as they developed during the two years of appellants' operations in Arizona with The French Shop, Inc., taken in consideration in connection with the very controlling factor that the Rices were the sole owners of the capital stock, the sole directors and the sole managers of the corporation, are sufficient to support the finding of fact that there was *FRAUD IN THE ORGANIZATION OF THE FRENCH SHOP, INC., FROM ITS INCEPTION.*

> This court has time and again decided that, where there is substantial evidence in the record to support the findings of the lower court, these findings will not be disturbed." (ITALICS ours).
>
> *Rice v. Sanger Brothers,* 27 Ariz. Rep. 15, 229 Pac. 397.

In order that the Court may have a clear picture of the fraud that has been perpetrated upon the people of Arizona, and especially upon the residents of Tucson and Phoenix, it is necessary to state some of the facts disclosed by the evidence in their chronological order.

Elsewhere in this brief, page 26, we have described the individuals who devised the fraudulent scheme and consummated the fraud to the extent of defrauding the public in a sum of approximately $190,000.00, and we have also set out their relationship to the bankrupt corporation and to the various corporations that have been used in the carrying out of the fraudulent schemes. (Pages 27-32 of this brief.)

Collating the facts and evidence in their chronological order, we find that the promotors of this scheme came from San Diego to Tucson about January, 1929 (T R 245) They found that Messrs. Mathews and Bilby, attorneys of high standing in Tucson, Arizona, had, at the instance of certain clients, filed Articles of Incorporation and prepared by-laws for the Arizona Holding Corporation. One of these individuals was Glen O. Perkins who became very active in the affairs of the bankrupt and of the Century Investment Trust subsequently. (T R 278).

The connection of Messrs. Mathews and Bilby with the corporation in question was short-lived, lasting only about a month. (T R 279). They had no connection whatever with the organization of the bankrupt corporation.

Under its permit to do business, the Arizona Holding Corporation was required to escrow all of its funds except such as paid for commissions on the sale of stock until it had raised the sum of $50,000.00 (T R 237). The funds were escrowed principally in the Consolidated National Bank of Tucson, Arizona. A tabulation of these deposits appears on page 276 of the Transcript of Record. It appears from this tabulation that the corporation in question was only able to sell stock sufficient to place in escrow the sum of approximately $36,000.00. (T R 236, 237,241,) $12,000.00 of which was deposited on January 23, 1929, and upon that date a non-operating loan was made and the funds deposited in this account in order to raise the sum on deposit to an amount in excess of $50,-000.00, (T R 273-276), and as testified to by Mr. Zapeda: "That was deposited in their account and made up a part of the total shown in the account of the Arizona Holding Company at the times the funds were released from escrow."

It was at about this time that this loan was made, namely, January 23, 1929, that Jesse H. Shreve first appears in the picture at Tucson (T R 245), and on March 4, 1929, he gave two cashier's checks of $5,000.00 each drawn on the California Savings & Commercial Bank of San Diego, California, and another check of $5,000.00 is-

sued to him in payment of this note. This transaction took place on the 4th day of March, 1929 (T R 274-275). At the time the loan was made the Arizona Holding Corporation had on deposit in this bank only the sum of $32,821.94. By whom the deposit of $12,000.00 was made on January 23, 1929, is not shown. These dates become important in view of the transaction immediately following which occurred at Prescott, Arizona, with the First National Bank of Prescott.

On March 7, 1929, Joseph E. Shreve, Jesse H. Shreve, J. G. Cash and Glen O. Perkins appear at the First National Bank in Prescott, Arizona, when Joseph E. Shreve, J. G. Cash and Glen O. Perkins each borrowed $10,000.00 from that bank (T R 204-206). Joseph E. Shreve, whose address was care Southwestern Union Securities Corporation, San Diego, California, gave his note to the bank for $10,000.00 endorsed by Jesse H. Shreve and pledged as collateral 100 shares of Sunset Building and Loan Association (of San Diego) stock, of the par value of $12,-500.00. This note was paid on October 9, 1929. (See photostatic insert at page 205 of Transcript of Record). Glen O. Perkins gave his note for a like amount, also endorsed by J. H. Shreve, and secured by 200 shares of the Security Building and Loan Association stock, (this corporation not being then organized.) This note was paid October 9, 1929. At the same time J. G. Cash made his note for a like amount, endorsed by J. H. Shreve, and secured by 100 shares of the Security Building and Loan Association stock, (this corporation not then being organized or having any permit whatever.) This note was also

paid on October 9, 1929. (See insert between pages 206 and 207 of Transcript of Record). Each of these notes was paid by check of the Security Building and Loan Association on October 9, 1929. On March 7, 1929, at the time of the execution of the three notes of $10,000.00 each, hereinbefore mentioned, the First National Bank of Prescott issued five certificates of deposit of $10,000.00 each, payable to the Treasurer of the State of Arizona, payable six months after date and signed by W. C. Evans, Cashier of the said First National Bank at Prescott, (See insert between pages 206-207 of Transcript of Record). Mr. Evans was also one of the incorporators of the Security Building and Loan Association.

In addition to the $30,000.00 in notes heretofore mentioned the First National Bank of Prescott received in payment of these certificates, a check drawn by the Arizona Holding Corporation for $20,000.00 (T R 233). This check was drawn upon the fund placed in escrow with the Consolidated National Bank of Tucson and on which the Arizona Holding Corporation had no authority to draw. The purpose of obtaining these certificates of deposit from the First National Bank of Prescott was to put them up in lieu of the deposit required by the State of Arizona before a building and loan association could receive a permit to organize. Section 628, Revised Code of Arizona, 1928. We see that the initial step in procuring this permission to organize was the securing of these certificates of deposit by a fraudulent transaction, namely, the giving to the First National Bank at Prescott in payment thereof an unauthorized and illegal check of the

Arizona Holding Corporation and the pledging of shares of stock in the bankrupt corporation without having at that time any permit to organize.

Immediately following this there follows a frantic telegraphic correspondence between Mr. E. T. Cusick, attorney for the Security Building and Loan Association in the matter of procuring the necessary release of escrowed funds from the Corporation Commission, the whole purpose of which was to prevent the $20,000.00 check of the Arizona Holding Corporation from being dishonored. The perpetrators of this fraud evidently depended upon Mr. Cusick to secure the release of the funds of the Arizona Holding Corporation during the period required for the transmission of the check from Prescott to Tucson. Accordingly we find (T R 233) a telegram on March 9, 1929, from Mr. Cusick to the Corporation Commission requesting the release of the fund and stating that formal application would follow by mail.

In petitioner's Exhibit No. 28 (T R 234) appears the telegram of Mr. McBride secretary of the Corporation Commission stating that the telegram is too indefinite and asking Mr. Cusick to state the reason why the money should be released and asking the question if the Holding Company intended to finance the Security Building and Loan Association, or what the money was to be paid for. On page 235 of the Transcript of Record appears Mr. Cusick's reply stating that the Arizona Holding Corporation had made loans and investments subject to the release of the fund; that "the Security Building

and Loan Association independent of other company has $50,000.00 up with the Banking Department. Stop. Please release funds before checks are dishonored. Wire release or telephone me immediately."

It will be noted here that the Corporation Commission was being deceived as to the fact that the check that was about to be dishonored was the $20,000.00 check of the Arizona Holding Corporation. On the same date (T R 233) Mr. Cusick wired the Commission as follows:

> "Please immediately wire release $20,000.00 Consolidated National Bank here. This must be here before three o'clock today."

Evidently the check given at Prescott on the 7th had reached the Consolidated National Bank on the 11th and no arrangements had been made for its payment. On that date the Corporation Commission evidently authorized the release of $20,000.00 by telephone and subsequently on March 18, 1929, wired a release of the remaining funds of the Arizona Holding Corporation (T R 236).

We think the inference is fair that in view of the kiting transactions of the promotors of these enterprises that these funds were released in order to make good not alone on the check to the bank at Prescott, but the cashier's check drawn on the California Bank in favor of the Consolidated National Bank. We have to bear in mind the relationship of these San Diego parties to the financial institutions at San Diego.

On page 237 of the Transcript of Record is shown

the letter of Mr. Cusick showing the aggregate sums of the Arizona Holding Corporation to be $56,580,27. This was contained in a letter dated January 24, 1929.

In Mr. Cusick's letter of March 14, 1929, (T R 238) it states that the Arizona Holding Corporation was then doing business and had opportunity to make loans and investments to advantage. On page 240 of the Transcript of Record he states that he was handed Articles of Incorporation and the Permit No. 6060 for Investment Company 2280 and the By-laws of the Arizona Holding Corporation.

The next step in the program of the Shreves and their associates was the incorporation of the Century Investment Trust and securing the permit for the sale of stock therein. This corporation appears later as the record holder of a large portion of the stock of the bankrupt corporation. It appears also as the transferee just before the state receivership of the bankrupt of practically all of the assets of the corporation. The practical identity of the control of the corporation is shown at various points in the evidence.

Having secured the corporate forms for their organizations on March 8, 1929, the promotors were all ready to proceed with their scheme for defrauding the public by the use of the mails and they sent out through the mails the circulars set up on pages 633 to 655, inclusive, of the Transcript of Record. The documents are remarkable and plausible, but there will be found no connection between them and the recognized business of a

building and loan association. They were well calculated to deceive the unwary. They have set up, as if they were endorsing the scheme outlined, the approval of President Herbert Hoover as to building and loan associations, quoting him at length. (T R 643). They set up also a similar letter from Ex-President Calvin Coolidge to a Mr. Howell (T R 646), a letter from Chief Justice Charles E. Hughes, then Secretary of State (T R 647), and then we have their own pictures of themselves:

"THE MEN BEHIND THE SECURITY

> The successful business leaders who are directors of this institution and investors in its guaranteed capital stock warrant the solidity, safety and success of the Security Building and Loan Association. Combine with them by depositing your funds in the Association."

These instruments were disseminated through the mails (T R 633-655).

On the insert opposite page 553 of the Transcript of Record is the schedule of commissions paid upon new accounts, and as Miss Young testified: "I saw the schedule actually used in the payment of commissions for new accounts." She further testifies that they were paid by the Security Building and Loan Association. These are very significant because the payment of a minimum of two per cent additional for the securing of these accounts made it impossible for the bankrupt corporation to ever carry out any of the representations it made to the public in soliciting these accounts.

The method of doing business of this bankrupt corporation and the conclusive evidence of the fraudulent purposes and character thereof, we think, is shown on that part of the Transcript on pages 312 to 317 inclusive, where are listed the loans made by the Tucson office. We use these as an illustration because they are typical of the rest of the business of this corporation. An examination of these pages of the Transcript of Record in connection with other parts of the record, which we shall point out, show that the entire amount of the loans placed during that period which cover those made up to 9/30/29, in amount $58,250.00, were made entirely for the benefit of the fraudulent corporations hereinbefore described and the promotors of this fraudulent scheme. We call the court's attention to this tabulation:

Loan No. 6 Overland Hotel & Investment Company (Arizona Holding Corporation Cr.)	$30,000.00
Loans Nos. 7, 8, 9 and 10, Century Investment Trust	15,500.00
Loan No. 4, Glen O. Perkins	3,500.00
Loan No. 3, Arizona Holding Corporation	1,000.00
	50,000.00
Loans 1 and 2, Purchase of mortgages from Helen Hannon (T R 313)	5,500.00
(Used for purchase of $5,000 stock in Arizona Holding Corporation. Petitioner's Exhibit 51)	
Loan No. 5, P. S. and Frances Burgess	2,750.00

(Moneys used on purchase of $4986.93 stock of Arizona Holding Corporation).

$58,250.00

These purchases are shown in Petitioner's Exhibit 51, Certificates No. 65, 67, 70, 71, (opposite page 531 of Transcript of Record).

It will be seen that every dollar of the funds of the Security Building & Loan Association realized through the fraudulent use of the mails or otherwise, found its way into the hands of the promotors of this scheme and the corporations organized and used by them for the purpose of defrauding the public. These exhibits further show that not one of these items was a loan within the contemplation of the Bankruptcy Act. They were principally purchases of mortgages; they were not loans to members of the corporations or to any person pretending to be members thereof and the purchasers were defrauded by being given stock in fraudulent corporations, the money being procured from the Security Building and Loan Association for the purpose of purchasing said stock and the promotors thereof taking the securities and then dumping them upon the Security Building & Loan Association, Bankrupt.

Similar transactions occur all through the career of this corporation. Illustrations will be found in the Transcript of Record at pages 79, 86, 313, 319, 339, 349, 350, 531.

We will ask the court to notice the wide discrepancy

between the dates in which the bankrupt corporation started its business and the date of its making any loans.

Revealing the true character of this corporation are the dealings that took place between it and the First National Bank of Prescott, Arizona, to which reference has heretofore been made. The First National Bank of Prescott issued to the State Treasurer five certificates of deposit for $10,000.00 each on March 7, 1929. Later on September 23, 1929 and October 9, 1929, these certificates were deposited to the credit of the bankrupt corporation with the First National Bank of Prescott (T R 205), and on the same date, October 9, 1929, the individual notes of Shreve, Perkins and Cash were paid to the First National Bank of Prescott by drawing from the account of the Security Building and Loan Association $30,000.00 in the form of a check to that bank. (See insert opposite page 205 of Transcript of Record and the testimony of Mr. Miller on that and succeeding pages).

From the above it will be seen that the bankrupt never received any benefit so far as the operation of the corporation was concerned from this $30,000.00 item, the money having been paid out in payment of said notes on the same day that it was deposited with the bank.

While the capital stock of the corporation is reported at times to be $40,000.00 and at other times $45,000.00, apparently the amount actually was $40,000.00 and all purported to be paid for. $30,000.00 of the purported capital having been withdrawn in the manner above shown, we further find (T R 205 and insert) that $9,000.00 more

was withdrawn by a check to the Arizona Holding Corporation. (T R 663-664). The rest of the funds included in the $50,000.00 originally raised on these certificates was dissipated in various ways. Owing to the disappearance of the records of the corporation, it is impossible to give a detailed statement thereof. Enough is shown, however, to show that $2,500.00 thereof went to the Sunset Building and Loan Association of San Diego (Insert opposite T R 205). In all probability the balance thereof went to the Arizona Holding Corporation first and then to the Shreves and their associates. We think that this is the natural inference from all the circumstances of the case.

We think too, that the evidence as herein stated, demonstrates that the issue of the capital stock to the Arizona Holding Corporation was entirely fictitious and without consideration; that it was never paid for as it was purported to be, and that the corporation received no benefit therefrom. However, as it was sending out the circulars hereinbefore referred to, paying the commissions for the securing of "deposits", it received a large sum of money and as we have shown, this, to the extent of approximately $190,000.00 immediately went into the pockets of the promotors so that we have up to this period not a single honest transaction by the bankrupt corporation, nor one that could by any stretch of the imagination be classed as a building and loan transaction.

In the report of the Bank Examiner (T R 317) occurs the following language:

"The above loans fail to qualify in almost every

particular under Section 618, Revised Statutes of Arizona, 1928 (Section 7, House Bill 162, Seventh State Legislature).

"A careful examination of each note, mortgage, fire insurance policy and other more or less important papers relating to each loan should be made at once for the protection of the Association's interests as a corporation, rather than leaning on and entangling with the interests of a holding corporation."

Unfortunately the Banking Superintendent failed to heed the advice of his examiner. On page 325 of the Transcript of Record appears the criticisms of this same examiner made January 13, 1930, in his report to the Banking Department. He reports no evidence of appraisal in the file of many loans and none signed by more than two appraisers. The law requires three. The Articles of Incorporation state $45,000.00 capital stock subscribed and fully paid for but the records show only $40,000.00; stubs of outstanding stock certificates not receipted; interests of the Association and Holding Corporation not clearly divided and defined. Assets of the Association and all equity therein should have clear and unquestionable title; no intermingling or partial transfer of propery rights.

From the time of this report up to the time of the appointment of the State Receiver on November 16, 1931, this corporation continued its fraudulent scheme of obtaining money through the fraudulent use of the mails and other fraudulent schemes and dissipating it in the same manner as we have heretofore pointed out. How-

ever, as appears from the evidence, Mr. Button ceased to be Bank Examiner subsequent to June 30, 1930, and Mr. Ellery succeeded him in that office. Mr. Ellery's examiners discovered such a state of affairs that he immediately telegraphed on November 10, 1931 (T R 290) to John C. Hobbs, vice-president of the bankrupt corporation, as follows:

> "From receipt of this wire hold all deposits made with your company intact and do not credit on current business. Stop. Confirmation by mail.
>
> S. W. ELLERY,
> Superintendent of Banks".

and on the same date (T R 290) he wired J. H. Shreve, Palace Hotel, San Francisco, California, as follows:

> "Unless conditions with which you are familiar are remedied in your Association at close of business by Saturday 14th inst., will ask for Receiver.
>
> S. W. ELLERY,
> Superintendent of Banks"

and on the 16th inst., before the Banking Department could act, a receiver was appointed in the State Court on complaint and appearance of bankrupt corporation, all taking place in the same forenoon.

Starting on page 298 of the Transcript of Record is the examiner's report upon which Mr. Ellery notified the bankrupt that he would close it up.

The comments and criticisms of Leo N. Roach, chief

examiner, and A. G. King, examiner, appearing on pages 373 to 375, inclusive of the Transcript of Record, are revealing and show in succinct form the fraudulent character of the bankrupt corporation. We quote from the high places:

> "c—From all appearances appraisals are made to evade the law, and fit the loans, instead of requiring the loans to fit the appraisals, and conform with the law.
>
> "d—Loans 41 and 42 in the Phoenix office, aggregating $66,000.00, secured by 240 acres of land near Wellton in Yuma County are accompanied by appraisals signed by Messrs. A. C. Shreve, Glen O. Perkins, and D. H. Shreve to the effect that the land is worth $150,000.00 and the improvements consisting of two frame dwellings to be worth $9,500.00 additional. The records of Yuma County Assessor's office disclose this assessed at $2,400.00 or $10.00 per acre, and nothing for the improvements. These two loans were set up to replace other questionable assets as outlined on page 15 of this report and must be eliminated at once.
>
> e—Loan No. 24 in Tucson office carried at $15,625.-00 represents an old loan of $6,000.00 on which the Association foreclosed and received a Sheriff's certificate of title in April, 1931. The Association later paid off a second mortgage held by the Century Investment Trust for $8,500.00, together with interest and costs, making a total of $15,625.00. This is a very unusual proceedure, and the item in question must be reduced to the amount of the original first mortgage, plus accrued interest and costs.

j—The Century Investment Trust and the Arizona Holding Corporation which own all the capital stock of this Association, with the exception of the qualification stock of five directors, appear to have derived untold benefits from practically every real estate loan standing on the books, either from the transfer of mortgages, the sale of property, or by the writing of insurance."

The above report was made after a three day examination. Necessarily the examiners could only make a superficial examination.

The facts leading up to this report to the Banking Department and the subsequent action of the Superintendent of Banks in ordering Jessie H. Shreve and his associates to stop taking in money for the bankrupt was caused by the nature and conduct of the business of the bankrupt. It would make this brief too long to set up all of these transactions or point out the fraudulent nature of each. Therefore we will point out only some of the high lights showing the Court that an examination of the record will show that the transactions in general will bear out the illustrations that we give.

One of these is shown on page 339 of the Transcript of Record, Loan No. 24, dated 6/11/31. This is what is known as the Silver Slipper transaction, the Silver Slipper being a notorious night club near Tucson, and by means of this transaction which fully appears on page 339 of the Transcript of Record, it developed that the bankrupt estate was defrauded in a loan of $15,625.00 for the benefit of the Century Investment Trust. This

incidently links up the connection of Oscar H. Robson with the bankrupt and with the Century Investment Trust.

On pages 628 and 629 of the Transcript of Record appear the minutes of the special meeting of the Board of Directors of the bankrupt corporation, signed by Glen O. Perkins as secretary, in which it is stated that a proposition had been made by the Century Investment Trust that the bankrupt release as collateral to the note of $250,427.45 the following mortgages then held by the bankrupt, towit:

Loan No.	37	A. W. and Fannie York
" "	41	Lyda Dreyfus
" "	42	F. D. Arrington
" "	44	Jas. M. Shumway
" "	53	Charles J. and Lucille Pinney
" "	59	G. W. and Susan E. Shurts
" "	60	Nancy Belle Flippin
" "	67	H. W. Durham

and accept as collateral in lieu of said mortgages, real estate covered by same. These notes and mortgages represented an aggregate, including interest of $113,945.84. Deeds therefor were made to the Arizona Holding Corporation not to the bankrupt, and as a result thereof there disappeared from the assets of the bankrupt these notes and mortgages of the face value of $110,406.58 principal sum, and including interest $113,945.84. Each and all

of these loans were false and fictitious and made upon false and fictitious appraisals by the parties who had conspired to defraud the public through means of the bankrupt corporation. These notes and mortgages are fully described in the Transcript of Record at pages 349 to 359 inclusive. They include the notes of Lyda Dreyfus and F. E. Arrington amounting to $66,000.00 on the 240 acres of desert land in Yuma County of a value not to exceed $2,400.00. It includes the $9,715.00 extracted from the funds of the bankrupt corporation by means of an entirely fictitious mortgage and note and which James M. Shumway, an employee, was deceived into signing, and the money was paid out in the form of two checks to James M. Shumway which he never saw, but on which his name was endorsed, and the subsequent endorsement of the Century Investment Trust which got the benefit of this transaction.

On pages 368 and 369 of the Transcript of Record appears the statement of the Dreyfus and Arrington Transaction, and the transfer of the funds thereon to the passbook credit of the Century Investment Trust No. 5226, showing the fraudulent nature of the transaction and the disposition of the $66,000.00.

In the testimony of Mr. James A. Smith, certified public accountant (Tr. 663) this whole transaction is traced from the inception of the corporation to its closing act in the cancellation of the mortgages.

But one purpose could have animated the perpetrators of this scheme in having these mortgages released

and that was to prevent the courts from ever ascertaining the true character of the transactions, and by releasing the mortgages and accepting deeds therefor to prevent prosecutions for the wrongful embezzlement of the moneys involved.

On October 1, 1931, the bankrupt corporation transferred practically all of its assets to the Century Investment Trust, accepting a note therefor of $250,-427.45 (T. R. 629). The undoubted purpose of this note was to further cloud the record and prevent the unfortunate people who had left their money in the hands of these schemers without any recourse whatsoever. Only the bankruptcy proceedings has enabled them to save anything from the wreckage caused by these fraudulent transactions.

In the minutes of the meeting of the Board of Directors of the bankrupt shown on pages 626 and 627 of the Transcript of Record occurs the following statement:

> "The question of divorcing the activities of this association from those of the Century Investment Trust was then submitted for discussion. It was agreed that this separation of activities would benefit the Association, and upon motion duly made, seconded and carried, the following resolution was adopted:
>
> RESOLVED That in furtherance of the best interests of this Association, its activities shall be separated from those of the Century Investment Trust in the future, in so far as possible."

Having called the Court's attention to a few of the high lights of the fraudulent schemes which the bankrupt corporation was organized to further, we leave this phase of the subject.

SPECIFICATION OF ERROR NO. II.

(Assignments of Error IV and V)

The findings of fact and conclusions of law appear on pages 183 to 191 of the Transcript of Record.

No additional findings were requested and no assignment of error is made pointing out any evidence to sustain this specification or the two assignments of error IV and V.

We think that it was the duty of counsel for appellants to point out the evidence which would show that a part of the business was a building and loan business, if that is their claim. Not a single transaction of a building and loan character is pointed out in their argument under this specification. They content themselves by a long argument on matter entirely irrelevant to this assignment. The only claim they make as to the doing of any building and loan business is that they deposited certain securities with the State Banking Department as required by law for the purpose of procuring a license to organize as a building and loan association and subsequently substituted a $50,000.00 surety bond for such securities. Just what could be claimed as the doing of a building and loan association

business by bankrupt we are at a loss to understand. Confessedly there was no mutuality in the corporation. The issuance and sales of certificates of indebtedness of any nature do not constitute the doing of a building and loan business and the same was held in

Lilley Building & Loan Assn. (C. C. A. Ohio) 285 Fed. 1020, affirming 280 Fed. 143.

The issuance of these certificates and the issuance of a so-called pass book certificate for funds payable upon demand were the only methods used by this corporation to obtain funds except by giving its promissory notes to banks from whom it borrowed money, hypothecating the mortgages of the bankrupt to secure the same. The form of these certificates appear on pages 217 to 219, inclusive, and the photostatic inserts between pages 220 and 221 of the Transcript of Record. In each of these instruments there appears this clause:

> "These certificates do not make the holder a member of the Association nor subject to any liability. They are non-assessable, nonforfeitable and are guaranteed by all the assets of the Association."

It does not appear from the evidence that any money was obtained upon any form of certificate other than those containing this clause (T. R. 218). The literature sent out by the bankrupt corporation is to the same effect. All the instruments are promises to pay and all the circulars exploit the accumulating force of compound interest. Nowhere was any building and loan literature sent out. The name was used to gull the unwary.

That purchasing of mortgages is not the doing of a building and loan business is held in

First National Bank v. Dawson, 213 Pac. 1097.
and in many other cases.

The lending of money secured by mortgages at a definite rate of interest and without the borrowers subscribing for any share in the building and loan association, is not the doing of a building and loan business.

Lilley Building & Loan Association v. Miller, Supra.

The receiving of deposits on demand or upon notice is not the doing of a building and loan association business and is an ultra vires act unless specifically authorized by statute. Such depositors are creditors, not members of the Association. This is the holding in

Acklin v. People Savings Assn., 293 Fed. 393.

We believe it needs no authority to support our contention that when, as is pointed out in this brief to be the fact here, the sole purpose of the corporation was the enriching of its promoters, and, to assist in that purpose, other fraudulent corporations were organized by those same promoters, which corporations were used as vehicles for carrying out such purpose through dummy loans and fraudulent transfers, and that all its business was done as part of the scheme and to further its unholy purpose, upon no theory and under no consideration can the business done by it be classed as the doing of a building and loan business.

That the promoters of this corporation never intended to do a building and loan business or to organize as a building and loan corporation appears from the circulars which they sent through the mails and otherwise distributed for the purpose of obtaining business and which were probably the principle factors in obtaining this business. For these circulars see Petitioners' Exhibits 78, 79, 80 and 81 (T R 633-654).

In discussing this assignment of error appellants cite cases to the effect that the provisions of the Bankruptcy Act enumerating the classes of corporations subject to the Act are to be strictly construed and include only such corporations as are clearly within the provisions of the act. Assuming that this is true, it is also true that the rule laid down by the Supreme Court of the United States is that no one can claim the benefit of an exception under a statute unless he comes strictly within the exception.

United States v. Dickson, et al., 10 Law Ed 689; 15 Peters 141.

Appellants' counsel do not seem very confident that the bankrupt is or was a building and loan association for They ask this Court to hold it to be a banking corporation if it does not find that it is a building and loan association. They do this despite the fact that every banking transaction, if it did any, would be ultra vires, and that no claim to the exception under the statute could be based upon an ultra vires transaction.

"Where the enacting clause is general in its

language and objects and a proviso is afterwards introduced, that proviso is construed strictly, and takes no case out of the enacting clause which does not fall fairly within its terms. In short, a proviso carves special exceptions only out of the enacting clause; and those who set up any such exception, must establish it as being within the words as well as within the reason thereof."

United States v. Dickson, supra.

"It is evident that appellee was organized to do a general savings and loan business, something less than either a bank or a building and loan association. If it occasionally engaged in banking transactions those acts were ultra vires and could not operate to make it a bank within the meaning of the bankruptcy law."

Clemons v. Liberty Savings & Real Estate Corp.
61 Fed (2) 448, (5th C. C. A.).

As the bankrupt corporation did not raise or obtain any money by the issuing of building and loan stock and as all the instruments under which it raised money expressly declare that the holders of such interest are not members of the corporation, it is very clear that it did not do any building and loan business so far as its receipts are concerned.

We now consider the other side of the picture, namely, the methods in which it invested its funds. As the Association by its Articles of Incorporation was precluded from issuing any membership stock or any building and loan stock, it necessarily follows that it could not do

a building and loan business so far as its investments and loans were concerned. The holding corporation was not qualified to be a member.

Morawetz on Private Corporations, Sections 431-433.

People ex rel Peabody v Chicago Gas & Trust Co. 130 Ill. 268.

Standard Savings & Loan Association v. Aldrich 163 Fed. 216 (6th C. C. A.).

Handelsman v Chicago Fuel Co. 6 Fed (2nd) 163.

Endlich, Building Associations 2nd Ed. 323.

Furthermore it does not appear that the corporation made any loans upon building and loan principles during its career.

Counsel for appellant seek to sustain their contention that the bankrupt is a building and loan association upon the theory that it is recognized as such by State Officials. We cannot see as a matter of reason that the fact that the promotors of a fraudulent scheme were able to deceive the officials of the Executive Department of the State, would be any res adjudicata of the proposition that they were not a building and loan association. Their contention merely is that the finding of a member of the Executive Department on an ex parte hearing is res adjudicata of the proposition and binding upon the Courts. The Supreme Court of the United States speaking through four different Chief Justices has answered that contention in the following cases:—

Chief Justice Hughes in Crowell v. Nelson, 76 Law Ed. 598; 285 U. S. 22-95.

Chief Justice Taney in Decatur v. Paulding, 10 Law Ed. 559, 14 Peters 497:

Chief Justice White in Kealoha v. Castle, Trustee, 52 Law Ed. 998; 210 U. S. 149-155.

The same was held by Chief Justice Marshall in an earlier case.

Counsel rely strongly upon the case of In re Humphrey Advertising Co., 177 Fed. 187. This decision was rendered under the old law when the principal business of the bankrupt determined its character. It has never since been recognized as the law and the Supreme Court of the United States distinctly laid down the contrary doctrine in a case decided by it some four or five days after that decision.

Toxaway Hotel Co. vs. Smathers & Co., 54 Law Ed. 558; 216 U. S. 439.

wherein the Court says:

> "Amenability to the statute must turn upon the facts of the case where, as here, the same corporation was engaged in "mercantile pursuits" in addition to inn keeping. There is no way to settle whether it was "engaged principally" in the one or the other but by comparison of the two. When we do this it is easy to see that the mercantile business which it did was of minor character, and was largely an incident to the location of the hotels of the company in a thinly settled mountainous region."

The Articles of Incorporation show that the bankrupt lacks the essential and fundamental characteristics of a building and loan association.

While we know of no case holding that the mere filing of Articles of Incorporation not followed by the user of the privileges set forth therein bring a corporation within any of the exceptions to adjudication under the Bankruptcy Act, we are firmly of the opinion that the Articles of Incorporation themselves show that the bankrupt is not a building and loan association within the meaning of either the statutes of Arizona or the common law of building and loan associations. Such associations are distinguished from ordinary corporations by having a form of stock that is payable on installments as distinguished from a form of stock that is paid-up capital from the start. This is an essential feature.

Wilkinson v. Mutual Bldg & Loan Assn., 13 Fed (2nd) 997.

Mutual Loan Association v Tyre, 81 Atl. 48.

Albany Mutual Bldg. & Loan Assn. v. City of Laramie, 65 Pac. 1011.

Towle v. American Building, Loan & Inv. Society, 60 Fed. 131.

In the case of Wilkinson v. Mutual Bldg. & Loan Assn. supra, the court says:

"What is the instrument in question?

We must take judicial notice of the Wisconsin law relating to building and loan associations. It is a

matter of common knowledge that as to such associations there are certain fundamentals: (a) That their purpose always has been to enable persons of moderate means, by small monthly contributions, to become home builders, and owners; (b) except occasional borrowings to cover emergencies, they borrow no money and have no business other than the accumulation of money from the sale of their shares, usually on monthly payments, to their members, and the lending of that money to their members, who wish to buy or build homes, so that the sole profit comes from the use by the borrowing members, of the money paid in by all the members on their respective shares of stock."

The alleged bankrupt could not have under its Articles of Incorporation any members for the reason that the Articles provide that its entire authorized capital shall consist of the ordinary stock of a corporation incorporated under the general law. For that reason the necessary mutuality does not exist to constitute a building and loan association.

Revised Code of Arizona, 1928, Sec. 612, Session Laws of Arizona 1925, Sec. 1, Chapt. 76.

Wilkinson v. Mutual Bldg. & Loan Assn., 13 Fed. (2nd) 997.

Western Bond & Mortgage Co. v. Crews, 231 Pac. 138.

Exhibits 10 to 23, inclusive (T. R. 212-221) show that the promotors of this corporation did not consider it a building and loan association or that it should have

members. The by-laws of the corporation also show a like intention, Article IX, Section 3, reading:

> "Holders of any of the forms of investment certificates above designated are not members of the corporation and have none of the rights, powers and liabilities incident thereto." (T. R. 72).

The bankrupt did not derive any money from the sale of building and loan stock. Consequently it could not comply with the provisions of the statutes under which it was incorporated nor with the general law of building and loan associations.

> *Western Bond & Mortgage Co. v. Crews,* 231 Pac. 138.

The Statutes of Arizona, Section 615, Revised Code of Arizona, 1928, provide that the government of a building and loan association shall be vested in its members. The Articles of Incorporation preclude this. See Article II, Section 2, of bankrupt's By-laws reading as follows:

> "The majority of the Board of Directors shall always be selected from those holding ten or more shares of the capital stock and the minority may be selected from holders of membership shares." (T. R. 63).

As the Articles made it impossible for the corporation to issue membership shares and as it actually did not issue any, it is clear that it was impossible for the bankrupt to be a building and loan association under Section 615 of the Revised Code of Arizona, 1928. As the statutes of

Arizona are practically the same as the common law of building and loan associations, it could not in any event be a building and loan corporation. As the only holder of any stock in this corporation was the Arizona Holding Corporation, a corporation, and as it was incapable of becoming a member of the association, this so-called building and loan association was without any members.

Morawetz on Private Corporations, Sections 431-433.

People ex rel Peabody v. Chicago Gas & Trust Co., 130 Ill. 268.

Standard Savings & Loan Assn. v. Aldrich, 163 Fed. 216 (6th C. C. A.).

Handlesman v. Chicago Fuel Co., 6 Fed. (2nd) 163.

Endlich, Building Associations, 2nd Ed. 323.

No presumption arises from the use of the name, Building and Loan Association. Calling a thing by one name when its organization and characteristics are something entirely different, does not make it the thing named.

Rhodes v. Missouri Savings & Loan Co., 173, Ill. 621.

Meroney v. Atlanta National Bldg. & Loan Assn., 116 N. C. 882, 47 A. S. R. 841.

Lilley Building & Loan Assn., 280 Fed. 143.

United States v. Freed, 179, Fed. 236.

Homebuilding & Savings Co., 12, B. T. A. 289.

Acklin v. Peoples Savings Bank, 293 Fed. 393.

The name of the corporation so organized is not ma-

terial if it has the purposes and characteristics named in the statute and its constitution.

Cramer v. Ohio L. & T. Co., 69 L. R. A. 415.

"The fact that a corporation calls itself a building and loan association * * * is not determinative of its true character, if the mutuality requisite to a building and loan association is lacking."

Home Building and Savings Co., 12 B. T. A. 289.

BADGES OF FRAUD AND PRESUMPTIONS THEREFROM

The proofs of fraudulent transactions introduced at the hearing before the Trial Judge and set up in the Transcript of Record are so numerous as to become conclusive, and in any event shift the burden of proof to the bankrupt to establish by clear and conclusive evidence that its transactions were fair and honest, and that its assumption of the name of a building and loan association was not fraudulent and not intended to deceive the unwary; that there was no fraud in its inception; and that it was honestly doing a building and loan business for the benefit of its members; that it was composed of members governed by members for the benefit of members.

Wait on Fraudulent Conveyances Section 225.

Toone v. Walker, 243 Pac. 147.

As the transactions between the interlocking direc-

torates of the corporations are presumptively fraudulent and as the evidence shows that these were actually fraudulent, the bankrupt can claim the benefit of no exception under the Bankruptcy Act.

Steinfeld v. Copper State Mining Co., 37 Ariz. 151, 290 Pac. 155.

Garden Development Co. v. Warren Ranch, 35 Ariz. 254, 276 Pac. 839.

As there was no user of any privilege of a building and loan association claimed for it under its Articles of Incorporation, the bankrupt is not a building and loan association.

Elgin National Watch Co. v. Loveland, 132 Fed. 41.

NATURE OF BUSINESS DONE AT TIME OF THE COMMISSION OF THE ACT OF BANKRUPTCY GOVERNS.

This corporation a month prior to the commission of the Act of Bankruptcy upon which it was adjudicated a bankrupt conveyed all of its property to another corporation (T. R. 628-629) and thereby abandoned all pretense of doing a building and loan business. It then stood revealed as a fraudulent monied corporation not coming within the exceptions of the Bankruptcy Act.

> "In view of the evidence, we are impelled to the conclusion that at the *time of the commission of the alleged act of bankruptcy* appellant was chiefly engaged in farming, and, such being the case, we are

of the opinion that the lower court was in error in adjudging appellant to be a bankrupt." (Italics ours).

Counts v. Columbus Buggy Co., 210 Fed. 748 (4th C. C. A.).

To the same effect are:

Flickinger v. First Nat. Bank, 145 Fed. 162 (C. C. A. 6th).

In re Inman, 57 Fed. (2) 595.

From the above it will be seen that the date of the commission of the act of bankruptcy determines the right of the bankrupt to claim an exception to the adjudication. In the instant case a month prior to the appointment of the State Receiver the bankrupt had abandoned all pretense of doing a building and loan business and transferred all of its assets except furniture, to the Century Investment Trust.

SPECIFICATION OF ERROR NO. IV.

Under this specification counsel for appellants assert that the Court had no jurisdiction to adjudge the appellant a bankrupt. This is based upon the theory that the District Court had no power to allow the amendment of the involuntary petition in bankruptcy and for that reason the case should be dismissed.

In support of this contention counsel cites two cases. The case of Norris v. Crocker, 14 Law Ed. 210, 13 How. 429, merely holds that where an action for the recovery

of a penalty prescribed in the Act of 1793 was pending at the time of the repeal, such repeal is a bar to the action. No question arose as to an amended complaint and in the nature of that case no amended complaint could have been filed that would have retained the jurisdiction in the court.

The case of Merchants Insurance Co. v. Ritchie, 18 Law Ed. 540, 72 U. S. 541, is merely to the effect that when the jurisdiction of a cause depends upon statute, the repeal of the statute takes away the jurisdiction. No question of the amendment of the complaint setting up facts existing at the time that the petition was filed was involved:

Also the Supreme Court of the United States has ruled upon the question in a clear cut decision where the sole questions involved were the amendment of an involuntary petition in bankruptcy to state jurisdictional facts not stated in the original petitions and relating to exceptions in the Bankruptcy Act and the method of raising objections on appeal. In the case of

Armstrong v. Fernandez, 52 Law Ed. 514; 208 U. S. 324-332

it was held that petitioning creditors had the right to amend a petition so as to aver that the bankrupt "is not a wage earner, nor a person engaged chiefly in farming or the tillage of the soil, and who is chiefly engaged in commercial business." The District Court made findings of fact and conclusions of law under General Order

36. The District Court gave the petitioning creditors leave to amend their petition and set up the jurisdictional facts as they actually existed. The Supreme Court speaking through the Chief Justice said:

> "The errors assigned in reference to the action of the Referee and of the Court in permitting amendments of the verification and other amendments, we regard as without merit. The power of a Court of Bankruptcy over amendments is undoubted and rests in the sound discretion of the Court. We think that there was no abuse of discretion here and the Court was fully justified in its order in reference to the amendments."

The other question involved in that case was raised by an assignment of error very similar to the one that is filed in this case. The appellants had appealed from the order of adjudication on the ground that "there is neither fact nor evidence that the alleged bankrupt had committed either the act of bankruptcy alleged, or any act of bankruptcy whatever." The Chief Justice in his opinion says with reference to this point:

> "From that order of adjudication this appeal was prayed but it nowhere appears that Armstrong and others objected to the want of proof of the acts of bankruptcy or asked any findings in respect thereto, or objected to the findings that were made for deficiencies in that regard. In other words Armstrong and others permitted findings to be made as they were and now say that other findings should have been made in relation to proof of acts of bankruptcy without having objected that they were not made, or

> that the findings as made were on that account fatal to the judgment. The presumption is that if such a suggestion had been made to the court the alleged deficiencies, if really existing, could have been supplied and would have been supplied."

The Chief Justice further along in the opinion states:

> "It seems clear that the acts of bankruptcy had been previously determined as committed, and that the case was only contested on the other point and hence that this contention is an afterthought which ought not to be entertained, let alone that from the findings that were made it is obvious enough that Alvarado was in liquidation and might properly be adjudged a bankrupt."

The decree was affirmed. We submit that the above cited case is conclusive in this matter. As in that case it appears that "from the findings that were made it is obvious enough that * * * might properly be adjudged a bankrupt", we see no necessity under this holding for the Court to go beyond the finding of that of the Trial Judge. It cannot be urged that this Court should go into the matter because it is a jurisdictional question, for it was a jurisdictional question in that case the same as it is in this; yet the Court held that the findings of fact were conclusive.

Other cases holding that an involuntary petition may be amended to correct errors in the statement of jurisdictional facts in the original petition are:

Gleason v. Smith, 145 Fed. 605 (C. C. A. Pa.).

State Bank v. Haswell, 174 Fed. 209 (C. C A. Iowa).

Massagli v. Butler Co. (9th C. C. A.) 16 A. B. R. (NS) 10, 39 Fed. (2) 346.

Millan v Exchange Bank (C. C. A) 183 Fed. 753.

International Silver Co. v. N. Y. Jewelry Co., (C. C. A. 6th) 233 Fed. 945.

Morrison v. Rieman (7th C. C. A.) 249 Fed. 97.

In re Cleveland Discount Co., 5 Fed. (2) 846 at p 858.

Mr. Graham Foster (now deceased), the attorney for the intervening petitioning creditors, on February 19, 1932, filed his verified petition for leave to amend the involuntary petition theretofore filed by him. (T. R. 46-47). In this he stated the facts to be "that your petitioners were misled by the name of said alleged bankrupt and by information received from various sources into believing that said alleged bankrupt was a building and loan association and was transacting business as a building and loan association and so alleged in their said petition. That since the filing of said petition, petitioners have learned from an examination of the officers of said alleged bankrupt and from other sources that said alleged bankrupt is not a building and loan association and was not engaged in building and loan association business", and prayed for leave to amend and file an amended involuntary petition, and on the same day the court made the order allowing the amendment of the petition (T. R. 48).

The court ,of course, had ample power to allow the

amendment. The petition set up adequate reasons why the petitioners should be allowed to amend. The subsequent evidence in the case demonstrates that the amendment was based upon facts existing at the time the original petition was filed but that had been fraudulently concealed from the petitioners and the public generally. No error has been predicated upon the allowance of this amendment by the District Court. We submit that it is not a question properly to be raised upon this appeal.

SUMMARY

It is apparent from the facts and evidence in the Transcript of Record, and which we have endeavored to point out in this brief, that the bankrupt corporation is merely:

1) A corporation organized to defraud the public by violation of the criminal laws of the State and Nation;

2) That at its best it is a mere loan company without any of the features of a building and loan association and incapable of doing the business of one;

3) That it never did any building and loan business of any nature;

4) That it was confessedly fraudulent in its conception and operation;

5) That it obtained a license as a building and loan association by fraudulent deception of state officials;

6) That upon the hearing on adjudication it failed to disclose to the court the actual situation and condition of the corporation.

IN CONCLUSION

NO CREDITOR INTERVENED TO OPPOSE THE ADJUDICATION:

It is significant that no creditor of the corporation ever intervened to oppose the adjudication in this matter or to maintain this appeal, and the bankrupt being confessedly insolvent and the assets not reverting to it under any circumstances, and as the corporation has no funds other than concealed assets out of which this expensive appeal could be maintained, it is apparent that the purpose thereof is to permit a tricky and dishonest creditor to escape the provisions of the Act and to enable its dishonest directors and officers to escape their just punishment.

> "This Act must be construed * * * to avoid an interpretation, unless the same be compelled by the language of the statute, which permits a dishonest or tricky debtor to escape its provisions."
>
> *Hills v. F. D. McKiness Co.*, 26 A. B. R. 329; 188 Fed. 1012.

It is also significant that in the face of all the fraud proved in the trial court, with serious charges involved against the honesty and integrity of the officers and directors of the bankrupt corporation, that not one of these

officers or directors was put upon the stand to refute the evidence that was adduced by the petitioning creditors and that no disclosure was made by them of the conduct of its affairs. This is conduct that no honest or upright person would permit to go uncontradicted into the record of a case in which he was a party or in which his honor was involved.

Upon all the record in the case, these appellees respectfully submit that the decree of the District Court adjudicating Security Building and Loan Association, a corporation, a bankrupt should be affirmed.

Respectfully submitted,

Alice M. Birdsall

ALICE M. BIRDSALL,

Counsel for Mary Rose, Ray L. Rose, Joe Ramos, Lillian M. Erwin, Luther M. Frink, E. Dale Frink, John H. Digges, Billie Lieber, Hattie M. Lieber, Hattie Schneider Lieber, Henry F. Lieber, Henry Lieber, Jr., Herman Lieber, Intervening Creditors, Appellees.

Thomas W. Nealon

THOMAS W. NEALON,

Counsel for R. E. L. Shepherd, Receiver in Bankruptcy, Appellee.